



**Bangladesh SMEs during the Pandemic:  
Coping with the Challenges and Mapping  
the Opportunities**

**Dr. Atiur Rahman**

Bangabandhu Chair Professor, Dhaka University  
Former Governor, Bangladesh Bank

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# Bangladesh SMEs during the Pandemic: Coping with the Challenges and Mapping the Opportunities

Dr. Atiur Rahman<sup>1</sup>

## 1. CONTEXT

Bangladesh as an economy has had a remarkable journey since its independence almost five decades ago. Development experts and economists have acknowledged its amazing macroeconomic achievements as well as its achievements in terms of humane development. It literally 'rose to today's prosperity from yesterday's ashes.' Especially, over the last decade or so the country has experienced a 'quantum jump' in terms of many development indicators and has successfully placed itself as a role model of sustainable and inclusive development for the rest of the world (developing and developed alike). And the ever-growing SME sector of the country can be attributed a (if not the) significant share of the credit for this success story which is still unfolding. Consequently, as the country was aspiring to become a high-income country within another two decades or so, development thinkers and policy makers have been emphasizing on greater need for sustainable development and management of the SME sector. Unfortunately, no one foresaw the looming danger of the on-going pandemic and the sub-sequent global economic slowdown. Undoubtedly, the global economy has not faced so sharp a contraction in living memory and it is still uncertain when will be the end to it. Since the surge of the infections remains unabated it is very difficult to anticipate what is in store for the global economy. The pandemic-induced global financial crisis, without any doubt, has also severely affected Bangladesh economy and the SME sector of the country been perhaps the most affected. In hindsight, SME sector being the largest employer in Bangladesh, can also lead the recovery process provided the sector gets timely, adequate and prudent policy support. The Bangladesh Government has, of course, declared a large stimulus package for the sector. The challenge lies in its judicious implementation as many of the SME entrepreneurs are new and work in the informal sector with no credible cash-flow management which is useful for the lenders.

### THE QUANTUM JUMP OF BANGLADESH ECONOMY

The stunning macroeconomic performance of Bangladesh over the last two decades is explicitly visible in terms of growth of the size of the economy. Between 2009-10 (Fiscal year of Bangladesh) to 2018-19 it has grown from 6 trillion BDT to 11 trillion BDT. Moreover, the economy of Bangladesh has also shown strong resilience to the global financial crisis that ensued by the end of the first decade of this new century. Besides targeting the overall economic growth strategy, there were several inclusive growth policies taken by the government which include a) extending digital connectivity of the economy under the banner of 'Digital Bangladesh', b) promoting policies of financial inclusiveness by the central bank for the disadvantaged smaller entrepreneurs and farming communities across Bangladesh, and c) extending the social safety net for the poorest. The prudent support for the climate affected vulnerable communities through innovative adaptation and mitigation strategies in addition to the pro-active sustainable finance strategy of the central bank also provided an extra edge to Bangladesh while pursuing climate

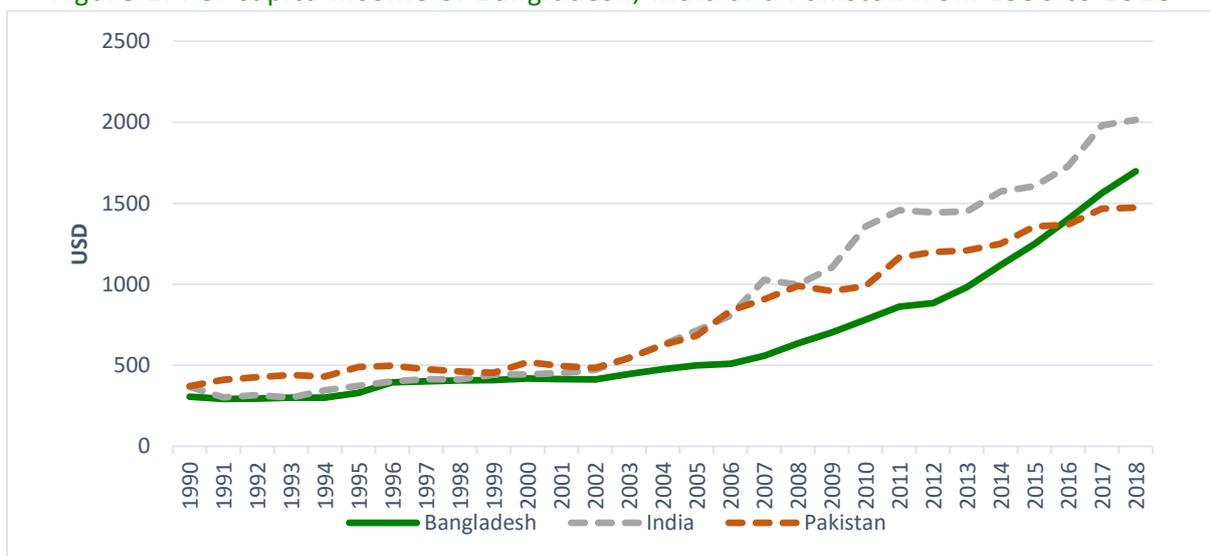
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<sup>1</sup> Bangabandhu Chair Professor, Dhaka University and former Governor of Bangladesh Bank. The author is deeply indebted to Abdullah Nadvi and Robert Shguvro Guda of Unnayan Shamannay for their excellent research support.

friendly sustainable development. Steady economic growth and many poverty reduction strategies adopted by the government of Bangladesh led to a continuous fall in the poverty rate of Bangladesh. At the same time, it is also predicted that if this growth pattern continues, Bangladesh will become the 26th largest economy of the world by 2030. Bangladesh has also achieved a lot both in terms of economic and social development indicators, and hence is being considered a model for inclusive development (Rahman 2019).

Rapid growth of Bangladesh economy naturally entailed similar growth in terms of per capita income. As shown in the next figure per capita income of Bangladeshis has been steadily rising from 306 USD in 1990 to USD 1,638 in 2016 (see Figure 1) and furthermore it has been rising at a rate faster than that of Pakistan and India. By 2018, per capita income of Bangladesh reached nearly USD 2,000.

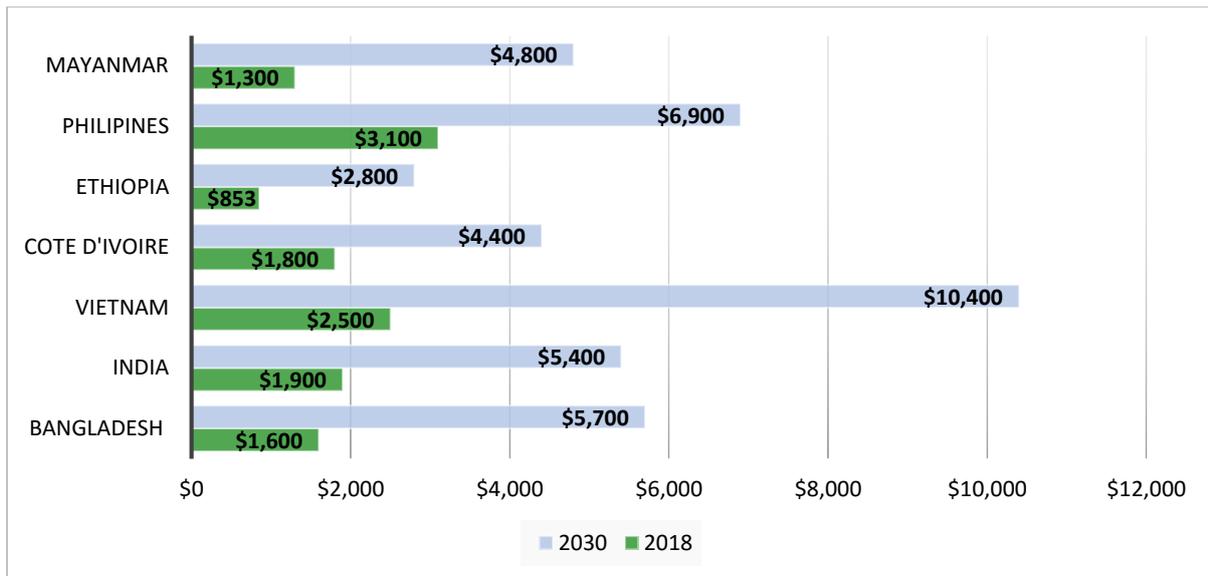
Figure 1: Per capita income of Bangladesh, India and Pakistan from 1990 to 2018



Source: World Bank data

HSBC Global Research (2018) projected that in between 2018 and 2030, Bangladesh’s GDP growth rate would be 7.1 percent per year on average. Consequently, according to these projections, by 2030 Bangladesh economy will be larger than that of the Philippines, Pakistan, Vietnam and even Malaysia (Henry and Pomeroy, 2018). The Asian Development Outlook of ADB (2019) put Bangladesh as the only country with eight plus percent of GDP growth in 2018. The outlook said that Bangladesh will remain the fastest growing country in Asia with 8.1 percent growth of GDP in 2019. The World Bank, on the other hand, predicts GDP growth to be less than the projection by ADB. However, the World Bank’s projection still puts Bangladesh at a more elevated position compared to its South Asian Peers.

Figure 2: Per capita GDP in 2018 and 2030, Bangladesh and other emerging economies



Source: Standard Chartered Bank, using World Bank, IMF and UN data

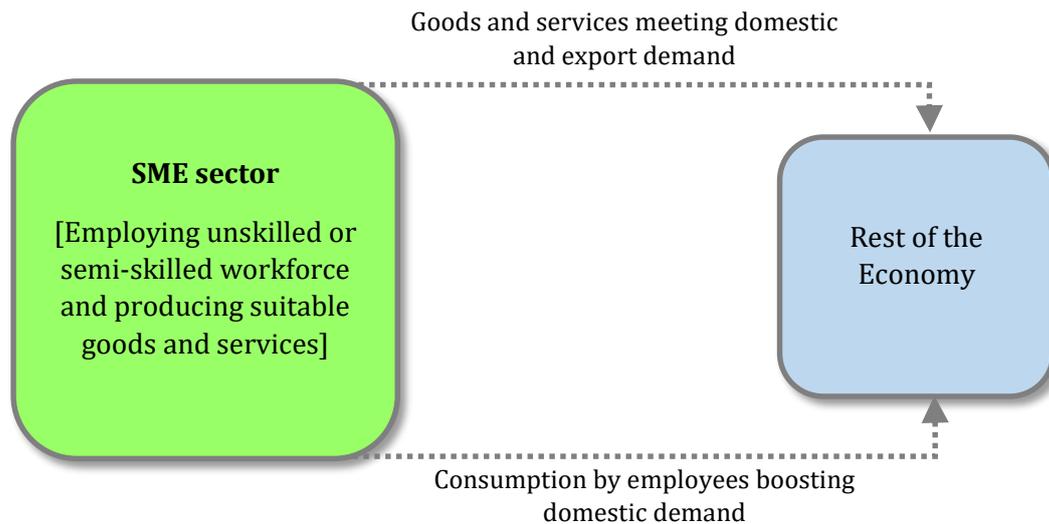
Figure 2 shows that in 2030, per capita income of Bangladesh (USD 5,700) will exceed that of India (Standard Chartered, 2019). Bangladesh's achievements in terms of different social indicators are even more impressive, with continued fall in infant and maternal mortality rates along with the highest life expectancy (nearly 73 years) in South Asia (Rahman 2019).

A number of factors have been contributing behind the country's macroeconomic success and these are expected to do so in the coming couple of decades as well. Bangladesh has been earning significant amounts of foreign exchange through RMG exports (commodity export boom) and as well as a few non-RMG items like ICT services, agro-processed, leather, ceramic and pharmaceutical products. It has also recovered well from the post Liberation War dislocations and consciously opted for inclusive development policies over the last decade or so for which the recent recovery could bounce back so quickly. The economy is currently enjoying the benefits of a broad-based financial inclusion campaign spearheaded by its central bank and strategically supported by the government over the last decade or so. As a result the access to finance has been enhanced to an unprecedented level (in fact, there has been a boom). And finally, Bangladesh is now looking to go beyond RMG export (export diversification) and focusing on attracting investments in other areas (the agro-processing industry is already doing very well). The planned special economic zones and ICT Parks could indeed be game changers in attracting FDI (Rahman 2020), particularly in the context of deepening US-China trade war forcing many foreign investors migrating out of China. As a result, Bangladesh has become the newest member of the so-called 7 percent club and the economy is poised to double in size by the end of the coming decade.

### ROLE OF SMES IN BANGLADESH ECONOMY

SME sector is said to be contributing 25 percent to the GDP of Bangladesh (Light Castle, 2020). This implies that the absolute amount contributed by this sector has increased more or less in alignment with the growth of the size of the economy (discussed earlier). However, macroeconomic significance of this sector is perhaps most explicitly visible through the sheer number of people employed in this sector. As per the Report of Economic Census 2013 by Bangladesh Bureau of Statistics (BBS), almost 8 million people are engaged in this sector.

Figure 3: Two-fold impact of SME sector on Bangladesh macroeconomy



Contributing a significant share of GDP implies that the SME sector supplies a significant share of the products and services consumed nationally and exported abroad. And employing (directly and indirectly) a very large share of the workforce implies that this sector ensures income for many households living at the bottom of the social pyramid. And these households in turn spend most of what they earn to buy goods and services and thus help boost the domestic demand. Hence, SME sector in Bangladesh contributes towards strengthening the supply-chain and as well as creates demand within the economy.

The SMEs have, thus, contributed significantly in macroeconomic success of Bangladesh through creation of employment for a rapidly growing workforce, value addition to gross domestic products, foreign exchange earnings and above all, reduction of poverty through creation of capital (SME Foundation, 2013). This also implies that in the coming decades as Bangladesh strives to become a high-income country this sector will continue to remain equally significant (if not more). And provided the diverse needs of this sector are addressed by the policy makers in a prudent manner this will go a long way in reshaping the economy of Bangladesh in the desired direction towards sustainable and inclusive growth trajectory.

### **COPING WITH THE PANDEMIC SHOCK**

The outbreak of COVID 19 across the world has resulted in a deepest global economic recession since the Second World War. The World Bank fears a 5.2 percent contraction in global GDP in 2020 (World Bank 2020). The Bank acknowledges the policy measures taken by the different Emerging Markets and Developing Economies (EMDEs) like Bangladesh and yet fears that per capita income in these countries will shrink in 2020 (ibid). Over the last decade or so, as Bangladesh went through a 'quantum leap' of macroeconomic development it has also become more integrated with the global economy. And so has the SME sector of the country. This implies that the booming SME sector of the country is facing (and will continue to do so in the coming few years) unexpected and unprecedented challenges because of the pandemic. On the one hand, possible medium- to long-term falls in demands will affect the sector. And on the other hand, overall deterioration of human capital formation may also adversely affect the sector's level of productivity.

In this context, this paper intends to map the policy measures that can help in sustaining the SMEs in Bangladesh during its process of economic recovery. This introductory section is followed by a brief presentation of the situation (challenges and opportunities) of Bangladesh SME sector in the pre-pandemic time. This is then followed by an analysis of impact of the pandemic on this

sector based on the information available so far. Finally, the paper investigates possible ways forward taking into account the policy measures taken so far, and good practices in other countries.

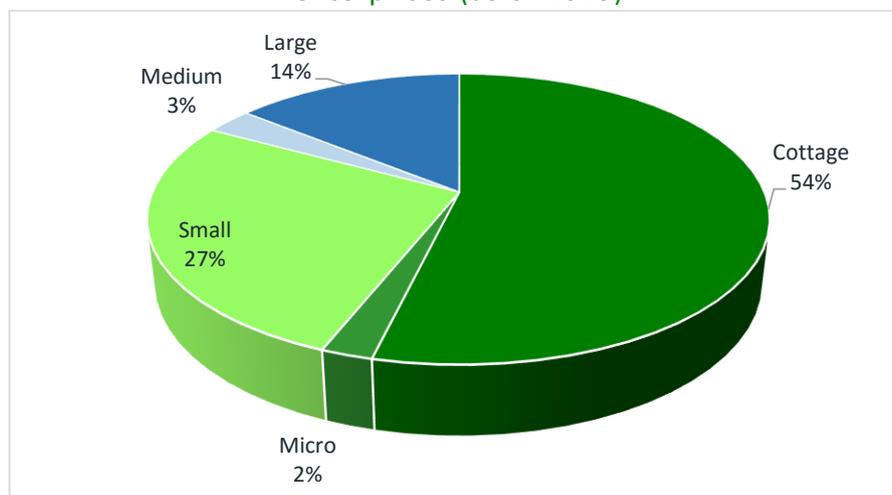
## 2. PRE-PANDEMIC SITUATION OF BANGLADESH SMEs

No doubt, there is an explicit policy level acknowledgement of macroeconomic significance of this sector and commitment to consider this as a core component of the national growth strategy. Yet, the official data generation on this sector remains quite scarce. However, the Report on Economic Census 2013 by BBS remains as the most recent comprehensive source of information related SME activities in the country. This section of the paper reviews the information from the said census report to portray overall picture of SMEs in Bangladesh. Additionally, more recent information from Bangladesh Bank related to SME financing are analyzed. Analysis of SME financing trend is done to portray the growing policy attention to this sector. Apart from this the core challenges facing SME sector (before the pre-pandemic period) are also discussed briefly. This is expected to facilitate better understanding of the new and/or additional challenges that the pandemic-induced economic slowdown has imposed on this sector. Finally, the National SME Policy 2019 of the Ministry of Industries, Government of the People's Republic of Bangladesh is reviewed briefly to present the national level planning and policy directives for this sector.

### SME SECTOR TRENDS

According to the Report of Economic Census 2013 by BBS, there were 7.8 million enterprises in Bangladesh at the moment and of them a staggering 6.8 million were cottage enterprises. The second largest group were the SMEs- over 866 thousand SMEs constituting just above 11 percent of all enterprises. Share of SMEs in the total employment created by enterprises is almost triple of their share in total number of enterprises (30 percent). As shown in the figure below small enterprises employed 27 percent of the workforce engaged in enterprises and the same ratio for medium enterprises is 3 percent.

Figure 4: Share (%) of enterprise workforce engaged in different types (size-wise) enterprises (as of 2013)



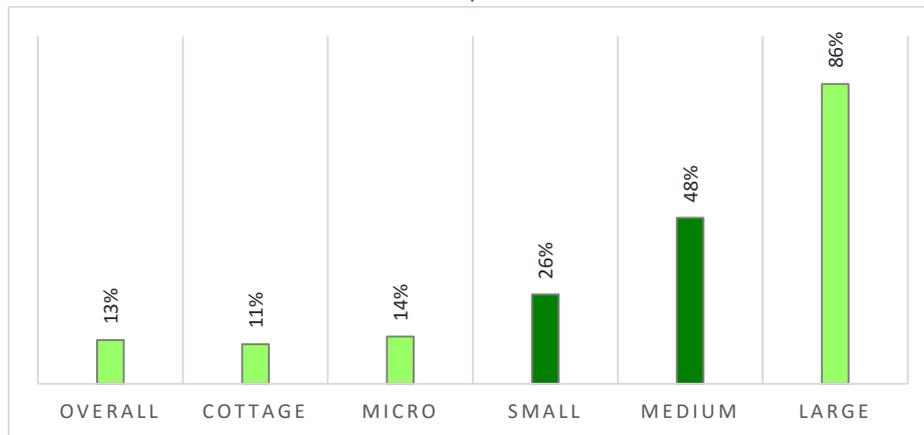
Source: Report of the Economic Census 2013, BBS

As of 2013, Bangladesh had over 868 thousand enterprises and of them over 109 thousand (13 percent) were exporting products/services abroad<sup>2</sup>. This ratio is significantly higher than the national average for SMEs. At the said moment, of the almost 31 thousand small enterprises- almost 23 thousand were exporting (26 percent). And of the almost 3 thousand medium enterprises- almost 16 hundred were exporting (48 percent). That is over a quarter of the small enterprises and almost half of the medium enterprises were earning foreign exchange through

<sup>2</sup> This is the sum of establishments that cater to international demand only and those which cater to both domestic and international demand.

exports. The ratio is higher (than SMEs) only for large enterprises which is only natural as large industrial units in the country are usually set up with the intention of exporting abroad.

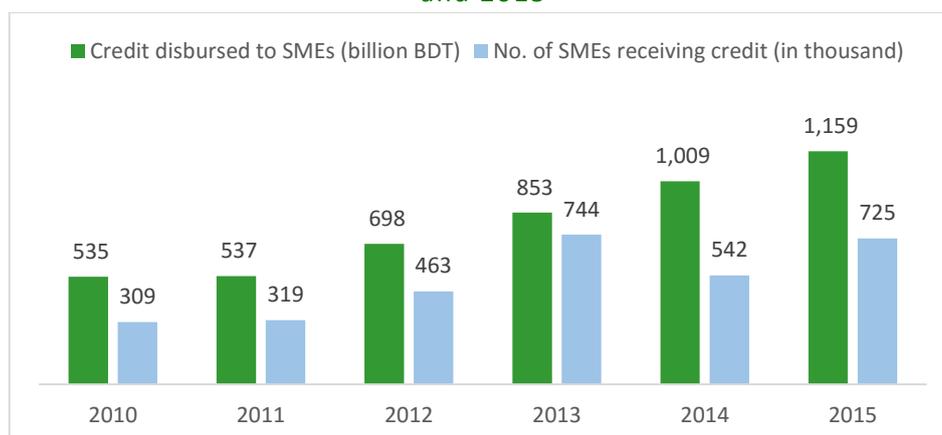
Figure 5: Share (%) of enterprises that are engaged in exports by different types of enterprises



Source: Report of the Economic Census 2013, BBS

Though not most recent, these information presents a clear picture of the pivotal role SME sector plays in creating employment and bringing in foreign currency for Bangladesh. The significance of SME sector has been acknowledged in a timely manner by the central bank of the country. And through numerous monetary policy innovations since 2009, SMEs have been being promoted extensively by Bangladesh Bank. Upon recognition of SME as a top-priority sector for rapid industrialization and poverty reduction, Bangladesh Bank opened a separate department titled “SME and Special Programs Department (SME&SPD)” in 2009. Special initiatives from Bangladesh Bank for SME sector promotion/facilitation included- a) setting up an indicative target for SME loan disbursement, b) following the “area approach method”, c) cluster development policy<sup>3</sup>, d) priority to the small entrepreneurs, women entrepreneurs, and e) special emphasis on manufacturing and service sectors (Aziz and Alom, 2019).

Figure 6: Credit disbursed to SMEs and number of SMEs receiving credit between 2010 and 2015

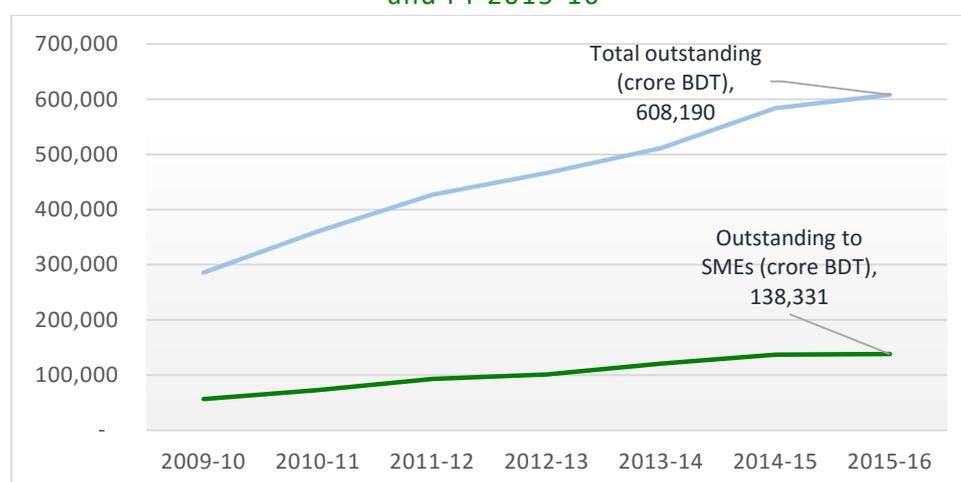


Source: Aziz and Alom, 2019

<sup>3</sup> With the intention of mapping the small industrial clusters across Bangladesh to formulate appropriate policies and SME development interventions SME foundation conducted SME cluster survey in 2013 and publicized the report.

The positive attitude of the central bank towards SME promotion is well reflected in the SME financing trend since the beginning of the current decade. As shown in Figure 6, both credit disbursed to SMEs through formal financing channel and the number of SMEs receiving those credits more than doubled within five years (between 2010 and 2015). During the said period, credit disbursed to SMEs increased from BDT 535 billion to BDT 1,159 billion and the number of SMEs receiving credit increased from 309 thousand to 725 thousand. However, it must also be noted that growth in SME credit disbursement could be even better. Between FY 2009-10 and FY 2015-16, share of SME credit and advances in the total outstanding has increased slightly from just below 20 percent to almost 23 percent. A sector employing 30 percent of the enterprise workforce should have received at least 30 percent of the credit disbursed for the sake of ensuring inclusiveness of the growth process. More importantly, the total outstanding has increased by an average BDT 53,761 crore per year. During the same period, average annual growth for outstanding to SME has been BDT 13,602 crore (see Figure 7).

**Figure 7: Outstanding credit and advances, overall, versus SME between FY 2009-10 and FY 2015-16**



Source: Aziz and Alom, 2019

## CHALLENGES FOR SME GROWTH

While SMEs in Bangladesh went through a commendable growth process since the beginning of current decade, as the sector continued to expand barriers to further expansion became increasingly visible. A sector assessment conducted by ADB under its Second Small and Medium-Sized Enterprise Development Project (RRB BAN 36200) identified certain impediments to desired growth of the said sector. These are: a) limited participation of women, b) centralization, and c) lack of access to finance (ADB, 2015).

First, less than one-third of the human resources engaged in the sector has been found to be women. And even when the micro-enterprises are taken into account the gender composition does not alter significantly. Hence, it will not be wrong to infer that if further female participation can be ensured through policy incentives then the sector is likely to grow at a more desired rate.

Secondly, though the economic census of 2013 showed that majority of the SMEs were located in the rural areas, it also showed that almost one-third of these SMEs were around the capital city of Dhaka and another 17 percent were around the second largest city-Chittagong. This is indicative of significant geographic disparities in terms distribution of

SMEs across the country. This clearly implies that there is significant scope of growth of SMEs in the other parts of the country.

Finally, and perhaps most importantly- lack of access to formal finance has been identified as a major obstacle on the way of survival and expansion of SMEs in Bangladesh. The factors (as identified by ADB) working behind have been found to be quite similar to other countries, namely- high lending rates; strict collateral and guarantee requirements; and complicated loan application procedures.

While the challenges discussed here are without any doubt prominent, the policy makers in Bangladesh have been diligent in addressing the same. For example, Bangladesh Bank (the central bank of Bangladesh) has come forward with numerous innovative policy directives/initiatives to support the sector in overcoming these barriers. These include- inclusion of all banks and NBFIs in the SME lending program; refinance window at bank rate for SMEs; guiding financiers to have separate CMSME financing strategy; Islamic shariah-based financing for CMSMEs, relaxation and revision of loan amounts for CMSMEs etc. (Aziz and Alom, 2019). The push for Women Entrepreneur Desk at each branch of the commercial banks by the central bank and earmarking a certain percentage of refinanced loan to the women entrepreneurs also indicate the gender-based developmental concern of the regulator. The Government of Bangladesh itself, of late, has come up with a clear long-term vision regarding SME sector development through formulation of the SME Policy 2019. This policy aims to strengthen the SME sector of Bangladesh by enhancing efficiency, improving business environment, providing easy access to finance, ensuring better marketing facilities, upgrading technology and innovative capabilities and creating employment opportunities (Ministry of Industries, GoB, 2019).

### **LOOKING AHEAD: SME POLICY 2019**

In alignment with GoB's macroeconomic aspirations for the coming couple of decades, SME policy 2019 and has set the target of increasing the contribution of the SME sector from 25 percent to 32 percent of GDP. The policy framework specifically emphasizes on development of sustainable environment-friendly SME sector and creation of an business environment where the SMEs may thrive at a desired rate with adequate infrastructural support, scope of innovative utilization of ICT, and effective coordinated participation of stakeholders from both public and private sector.

**Figure 8: Overarching objectives set in the SME Policy 2019 of GoB**



Source: Ministry of Finance, GoB

As shown in Figure 8, the latest policy related to SME development in the country has rightly emphasized addressing the major challenges on the way of desired growth of the sector in the coming decades. To attain these extensive SME development activities will have to be undertaken and that in turn will result in increased contribution of SME sector in the GDP and further reduction in poverty as a whole (Ministry of Industries, GoB, 2019). The policy document goes further laying out the strategic goals, sub-goals and actions to attain the goals/sub-goals. The next table shows the overall strategic framework of the policy.

Table 1: Strategies and actions proposed in the SME Policy 2019

Strategic Goal		Planned Actions
01)	Improving investment and business environment and institutional framework	<ul style="list-style-type: none"> <li>▪ Simplification of legal and administrative procedures</li> <li>▪ Rationalization of tax policy</li> <li>▪ Investment and revenue incentives for exporters</li> <li>▪ Enhanced coordination among stakeholders</li> <li>▪ Capacity building</li> </ul>
02)	Increasing scope of access to finance in SME sector	<ul style="list-style-type: none"> <li>▪ Creating a sustainable and effective institutional mechanism</li> <li>▪ Increasing amount of credit flow</li> <li>▪ Encourage innovation (SME Bank)</li> <li>▪ Strengthening existing refinance initiatives</li> <li>▪ Easy access to low-cost credit</li> <li>▪ Introducing credit guarantee schemes</li> </ul>
03)	Enhancing competitive capability and support to access of SME products into the market	<ul style="list-style-type: none"> <li>▪ Ensure quality of SME products</li> <li>▪ Facilitating capability building training</li> <li>▪ Provide advisory and information services</li> <li>▪ Enhance scope of entry to the export market</li> <li>▪ Domestic demand mobilization for SME products</li> </ul>

Strategic Goal		Planned Actions
04)	SME business support services, support to start-up businesses set up in a short period of time with low cost	<ul style="list-style-type: none"> <li>▪ Support to new businesses within short time and with low cost</li> <li>▪ Accessible start-up business process (online/digital system)</li> <li>▪ One-stop service for start-ups</li> <li>▪ Information and advisory services for start-ups</li> <li>▪ Collateral free loans for potential entrepreneurs</li> </ul>
05)	SME cluster-based enterprises network development and expansion	<ul style="list-style-type: none"> <li>▪ Improved infrastructure at BSCIC industrial estates</li> <li>▪ Incubation centers and Common Facilities Centers (CFCs) in industrial estates/clusters</li> <li>▪ Collateral free single digit rate loans for potential entrepreneurs in industrial estates/clusters</li> <li>▪ Increasing capacity and efficiency of entrepreneurs</li> <li>▪ Expand cluster development and business network</li> </ul>
06)	Increase the use of information, communication and other technologies	<ul style="list-style-type: none"> <li>▪ Promotion of modern, environment-friendly and energy-efficient technologies</li> <li>▪ Supporting expansion through e-commerce</li> <li>▪ Provide necessary ICT-based support</li> <li>▪ Establishing technology and innovation incubators</li> <li>▪ Promotion of automation</li> </ul>
07)	Expansion of skill development education and training programs for SME entrepreneurs	<ul style="list-style-type: none"> <li>▪ Developing and implementing appropriate business training programs</li> <li>▪ Developing standardized training modules and curricula</li> <li>▪ Enhancing capacity of training institutes</li> <li>▪ Developing online training content</li> <li>▪ Enhance coordination and communication among training providers</li> </ul>
08)	Extent programs for women entrepreneurship development and provide specialized services	<ul style="list-style-type: none"> <li>▪ Special training programs for women entrepreneurs</li> <li>▪ Increase flow of finance to women entrepreneurs (launching special development fund)</li> <li>▪ Capacity building of Women Chambers and the associated trade bodies</li> <li>▪ Awards and scholarships</li> <li>▪ Increasing market network and connectivity</li> </ul>

Strategic Goal		Planned Actions
09)	Establishing SMEs as effective linkage to large industry and protection of SME products	<ul style="list-style-type: none"> <li>▪ Developing linkage with large industry</li> <li>▪ Support for getting international certification</li> </ul>
10)	Development of capacity for establishing environment-friendly SME industries and industrial waste management	<ul style="list-style-type: none"> <li>▪ Encourage establishment of environment-friendly industry and provide necessary training</li> <li>▪ Provide training and incentives to improve waste management</li> <li>▪ Improve and increase use of environment friendly industrial technologies</li> <li>▪ Support for setting up waste re-cycling industries</li> </ul>
11)	Institutionalize SME Statistics and conduct research and development	<ul style="list-style-type: none"> <li>▪ Determine accurate contribution in national economy</li> <li>▪ Update SME related various indicators/statistics periodically</li> <li>▪ Conduct necessary research/investigation</li> </ul>

Source: Ministry of Industry, GoB (2019)

As shown in Table 1, the SME Policy 2019 is quite comprehensive and more importantly on the right track in terms of setting the strategic goals and activities to attain those goals. Moreover, these actions are time-bound, and the policy includes an action plan to implement and monitor these activities. These activities are to be completed by the end of FY 2023-204, and they are categorized as short-term (implementable within 1 year), medium-term (implementable within 2 to 3 years), and long-term (implementable within 4 to 5 years or more as necessary). The policy also clearly defines the roles of different actors (government and non-government) in materializing the said aspirations.

As far as pre-pandemic scenario is concerned, Bangladesh seems to have had a commendable growth pattern of the SME sector (especially visible through increased access to formal finance for the sector); a clear understanding/mapping of the core challenges on the way of further expansion; and most importantly, the country came up with a sector policy with clear cut objectives and a pragmatic action plan to attain the strategic goals. The pertinent question therefore is- to what extent the country needs to revamp its policy stance to cope with the affect of the ongoing pandemic on the economy as a whole and specifically on the SME sector itself. A pre-requisite to answering this burning question is a holistic assessment of the impact of the pandemic-induced economic slowdown as well as assessment of the outcome of the support initiatives already taken to safeguard the sector from the largest recession since the Second World War.

### 3. COPING WITH THE COVID-19 PANDEMIC

Over the past few months, on the one hand, Bangladesh as a country has been struggling to manage the health disaster caused by the outbreak of the pandemic (mostly because of the health sector not being adequately prepared to manage a shock of this scale). On the other hand, because of its deep integration into the global economy, the economy of Bangladesh has also been feeling the backlash of global economic slowdown (though not as severe as many other comparable economies of the world). Naturally, the SME sector of the country has also suffered due this massive crisis. Experts believe that this particular sector may be the most affected one because of its limited capital and shock absorbing capacity. While a comprehensive impact assessment is yet to be conducted (as the pandemic is still on-going and no one is sure when it will end); few quick empirical assessments have been conducted and the outcomes have been shared among the stakeholders. And GoB with potent and timely support from the banking system of the country has already launched stimulus package to safeguard the SME sector of the country (it has done so for other sectors as well).

This section of the paper presents the effect of the pandemic on the economy in general as well as on the SME sector based on the said impact assessment studies. It also attempts to assess the immediate effects of the stimulus package by GoB and map the challenges on the way of proper implementation of the stimulus program.

#### **PANDEMIC-INDUCED ECONOMIC SLOWDOWN AND BANGLADESH ECONOMY**

The most recent report on 'Global Productivity' from the World Bank published in the backdrop of the pandemic identified Bangladesh to be among the few economies that experienced a growth in productivity since the global financial crisis of 2008-09. As per the report, productivity growth in Bangladesh was robust between 2013 and 2018 at 5.1 percent (which is above the country's pre-GFC average productivity of 4.7 percent). This has put Bangladesh in the top decile of EMDEs. This success is attributed to macro-economic and political stability in the country that facilitated both public and private fixed investment (Dieppe, 2020). While Bangladesh has benefitted from its limited exposure to external headwinds, continued rapid urbanization, and an improving business environment, the COVID-19 shock and the related plunge in global economy poses significant risk to this productivity growth (ibid).

The World Bank, perhaps taking the afore mentioned risk into account, projected severely contracted growth for Bangladesh Economy in its latest report titled 'Global Economic Prospect', published in June 2020. The Bank projected a meager 1.6 percent growth of real GDP for Bangladesh in 2020 in stark contrast with the ratio being 8.2 percent for the previous year as per the Bank estimations. This projection, in fact, is 5.6 percentage points lower compared to earlier projections of the Bank for Bangladesh's real GDP growth rate in 2020 (World Bank, 2020). The Bank fears further cuts if bringing the pandemic under control takes longer than expected or if financial stress triggers cascading defaults (ibid).

The ADB, however, is comparatively much more optimistic about economic growth projection of Bangladesh in 2020 and 2021; and hence is closer to the predictions of GoB itself. In the Asian Development Outlook 2020, ADB especially focused on impact of the COVID-19 outbreak. It says that growth in South Asia will decelerate to 4.1 percent in 2020 and then recover to 6.0 percent in 2021 mostly in alignment with the trends in growth in India, the largest economy in the area. Yet, Bangladesh's GDP performance has been reported to remain strong. As per ADP forecasts, Bangladesh economy will grow by 7.8 percent (later adjusted to 6.8 per cent in September) in

2020 despite significant pulling back of global demand (ADB, 2020). This ratio is still 0.4 percentage points lesser than the growth recorded in the previous year (8.2 percent in 2019). ADB further projects that Bangladesh's growth rate will recover to 8.0 percent in 2021. And more importantly the report projects the inflation to remain in check and the current account deficit to further narrow during this period. In fact, it has already become positive, thanks to robust performances of the remittance and the export sectors in recent months defying earlier prediction of gloom by many experts and organizations. These optimistic forecasts about Bangladesh Economy by ADB rest on certain assumptions such as continuation of political stability, maintenance of consumer and investment confidence, improved trade in 2021, and expansionary monetary policy by the central bank to support economic growth. Most importantly, the ADB projections assume that the pandemic will not further affect economic activities of the country. It also identifies adequate resource mobilization through efficient taxation as the pre-requisite for Bangladesh to materialize its macroeconomic potential in the coming years (ibid).

While growth projections vary from one development partner to another, it is obvious that Bangladesh economy has already been severely affected by the pandemic-induced economic slowdown and a lot will depend in the coming years on how the policy makers deal with these affects. This is, perhaps, truer for the SME sector compared to the rest of the economy due to this sector being comparatively labor intensive, relying more on informal economic activities and above all- having comparatively lesser access to formal finance.

### **EFFECT OF THE PANDEMIC ON BANGLADESH SMES**

As has been mentioned earlier, a comprehensive assessment of the impact of the pandemic on the SME sector is yet to be conducted. This is partly because the pandemic is not over yet and partly because comprehensive and up to date SME statistics (data base) is not available. Yet, a couple of quick surveys regarding the effect of the pandemic on SMEs in Bangladesh has caught attention of the stakeholders. Bangladesh Institute of Development Studies (BIDS) conducted a quick survey covering 375 SMEs and 360 workers between 26 April 2020 and 10 May 2020 (Ovi, 2020). Key findings from the survey were:

- Average reduction of revenue for all SMEs is 66 percent in 2020 compared to 2019.
- Share of SME products remaining unsold due to economic slowdown was found to be 76 percent.
- Because of the 'partial lockdown' only 16 percent SMEs remained fully operational.
- Among the SME employee 42 percent received partial salary, while another 4 percent did not receive salaries at all.
- Entrepreneurs reported that they will be able sustain for about another month (i.e. until June 2020) if the lockdown continued further.

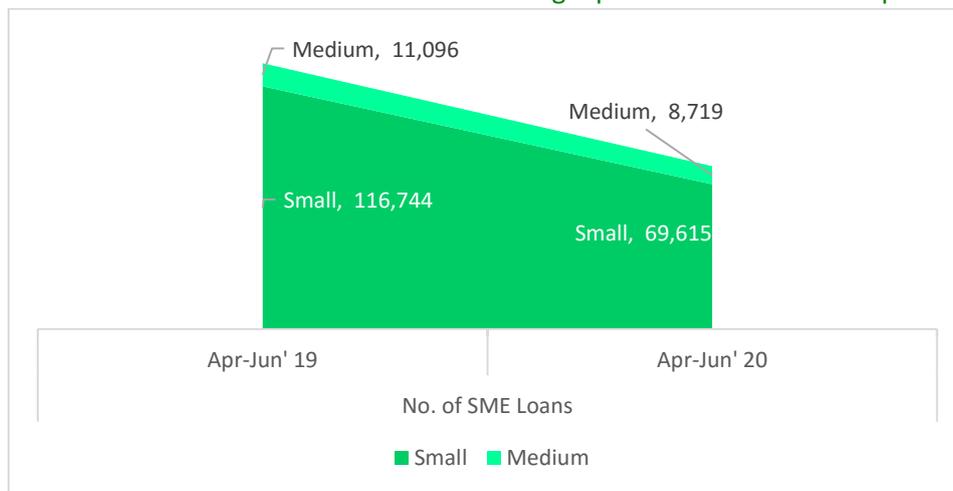
Another similar survey was conducted by LightCastle Partners in collaboration with Sheba.xyz which covered 230 enterprises across eight divisions of Bangladesh. This survey was conducted during the first week of April 2020. Survey findings revealed that many SMEs were unable to produce because of unavailability of raw materials during the partial lockdown. It also revealed that entrepreneurs were primarily reducing marketing and distribution expenses to cope with the losses, and service-oriented SMEs were facing greater challenges compared to other SMEs (LightCastle Partners, 2020). Other major findings from this survey were:

- 52 percent of the surveyed SMEs had to completely shut down operations.

- 28 percent of the entrepreneurs experienced drastic decrease in income (by over 50 percent).
- 68 percent of the entrepreneurs would not be able to sustain their ventures if the partial lockdown continued for over 4 months (i.e. up to mid-July 2020).

While these are findings from quick surveys conducted over relatively smaller sample sizes, their findings still are indicative of the severity of effects of pandemic on Bangladesh SMEs. A more precise picture can be drawn through comparison of SME financing trends of the second quarter of the current year (i.e. April to June 2020)<sup>4</sup> with the same trend of the second quarter of the previous year (i.e. April to June 2019). Of course, formal financial service providers still cover a relatively smaller share of the total number of Bangladesh SMEs. But still, a comparison of formal credit flows to this sector can be a suitable proxy indicator to measure the aggregate downfall.

Figure 9: Number of SME loans disbursed during April-June 2019 and April-June 2020

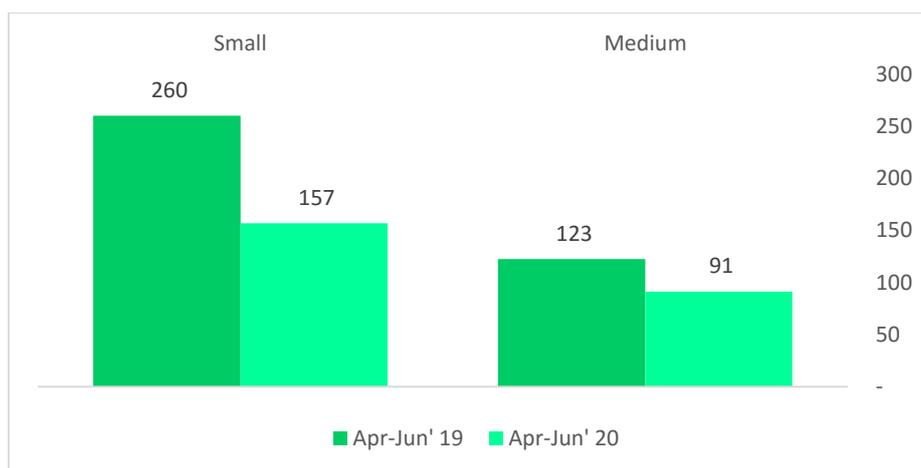


Source: Bangladesh Bank

Figure 9 shows that number of loans disbursed to medium enterprises came down from over 11 thousand to just below 8 thousand from the second quarter of 2019 to the same period of 2020 (a 21 percent decrease). The decrease is almost double for loans disbursed to small enterprises (40 percent). Loans disbursed to small enterprises came down to over 69 thousand in 2020 from over 116 thousand in 2019.

Figure 10: Amount (in billion BDT) of loan disbursed to SMEs during April-June 2019 and April-June 2020

<sup>4</sup> This quarter is chosen as Bangladesh went for partial lockdown in late March 2020 and started opening the economy in early August 2020.



Source: Bangladesh Bank

A similar pattern of drastic decrease is visible from early 2019 to early 2020 in terms of total amount of loan disbursed in favor of SMEs. Figure 10 shows that amount of loan disbursed to medium enterprises came down by 26 percent from April-June 2019 to April-June 2020 (from BDT 123 billion to BDT 91 billion). Here again the decrease is significantly higher for small enterprises- 40 percent (from BDT 260 billion to BDT 157 billion).

Both the figures (Figure 9 and Figure 10) indicates severely contracted demand for SME credit which is most likely due to slowing down of SME activities amid the outbreak of COVID-19. This implies that- on the one hand, SMEs in Bangladesh have been forced to remain non-operational because of the pandemic-induced economic slowdown, and on the other hand, entrepreneurs (old as well as new one) have been reluctant to take up new loans to expand and/or sustain their SMEs due to lack of confidence amid wide-spread uncertainties.

### **STIMULUS FOR SMEs: TIMELY AND FLEXIBLE APPROACH**

Commendably, GoB has been quick to take action to safeguard SME sector from the effects of pandemic-induced economic slowdown. The honorable Prime Minister declared a gigantic stimulus package worth BDT 20,000 crore for SMEs on 05 May 2020. One must also acknowledge other packages like Taka five thousand crore for the farm sector, three thousand crore revolving package for the vulnerable entrepreneurs belonging to the MFI sector, the pre-shipment credit of another five thousand crore are also meant for SMEs of various kinds including the modern farmers involved in poultry, fisheries and livestock enterprises. And Bangladesh Bank was also quick to come up with circular with clear directives to Banks and NBFIs regarding how to implement the said stimulus package for SMEs (SMESPD Circular 01 of Bangladesh Bank, 13 April 2020). The stimulus package intends to provide special working capital facility for CMSME under the financial incentive package declared by GoB. Key characteristics of the stimulus package (as per the original circular of SMESPD, Bangladesh Bank dated 13 April 2020) are given below:

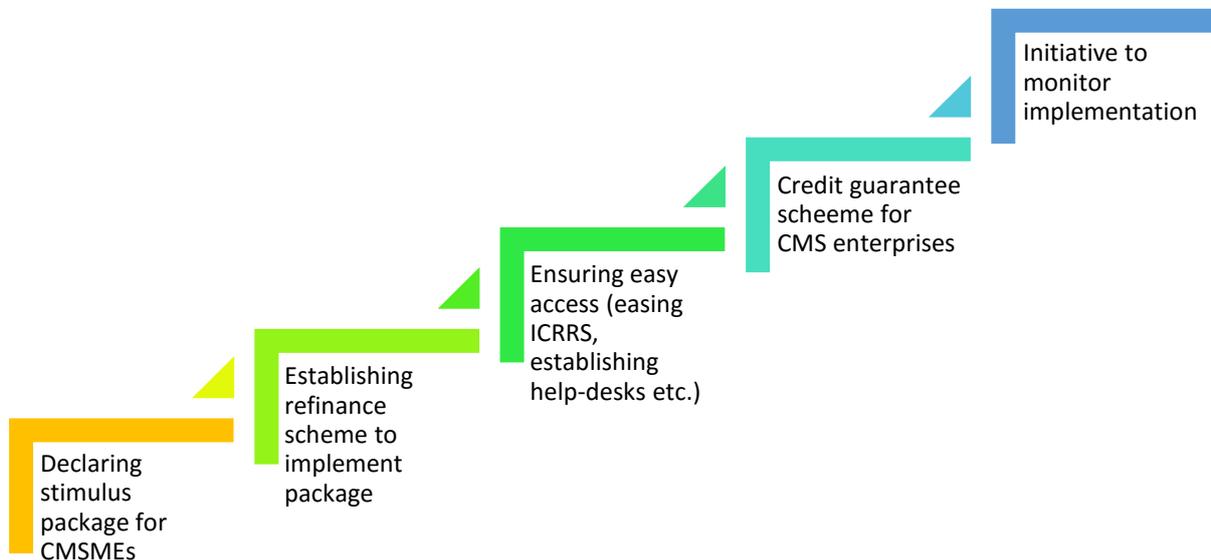
- Enterprises receiving loans under this package are to pay 4 percent interest and another 5 percent is to be borne by GoB (making the overall interest rate 9 percent).
- Banks and NBFIs are allowed disburse loans equivalent to 10 percent of their total CMSME outstanding loans under this stimulus package.
- While manufacturing and service-oriented CMSMEs are to be given priority in implementing the stimulus package, trade-oriented CMSMEs are also eligible to get loans under this package.

- 30 percent of the loans given under this package are to go for medium enterprises, while the remaining 70 percent are to go to the cottage, micro and small enterprises.
- 15 percent of the loans given are to go to rural CMSMEs and 5 percent of the loans are to go to women CMSMEs.
- While the package will be available for 3 years a single entrepreneur will be eligible only once to get a 1-year loan under this package.
- Only pandemic affected CMSMES are eligible for these loans and they will be selected based on bank-customer relationships.

While the provisions of the package are obviously timely and pragmatic (given the existing macro-economic situation), Bangladesh Bank went ahead with a flexible approach to ensure that implementation of the stimulus for CMSMEs remain demand-driven and contextual. As a result, the central bank, since mid-April 2020 has come up with 11 more circulars related to implementation of the CMSME stimulus package.

The point to be noted here is that the first circular from Bangladesh Bank regarding CMSME stimulus package implementation came out in a somewhat spontaneous manner (fueled by urgency to take potent actions to safeguard the sector). As the lockdown continued and financial service providers attempted to implement the package new challenges emerged. To cope with the emerging challenges, Bangladesh Bank resorted to making additions/revisions to the original circular to address those issues.

Figure 11: Flexible regulatory approach in implementing CMSME stimulus package by Banks and NBFIs



Banks and NBFIs were found to be not adequately interested to finance CMSMEs even before the pandemic. Hence, it was highly unlikely that their interest to provide CMSME finance would increase amid the pandemic (because even under this package the borrowers will have to be able to pay 4 percent of the 9 percent interest rate). To encourage the Banks and NBFIs to take this risk, Bangladesh Bank established a revolving refinance scheme to supply liquidity to Banks and

NBFIs especially so that they may have enough to lend to the CMSMEs under the said stimulus package.

The central bank has been equally attentive to the interests of the smaller borrowers. Hence, through multiple circulars the central bank directed the financiers to make the process of accessing CMSME credit as easy as possible. These directives included easing of Internal Credit Risk Rating System of Banks (ICRRs), setting up special helpdesks for borrowers seeking credit under this stimulus package.

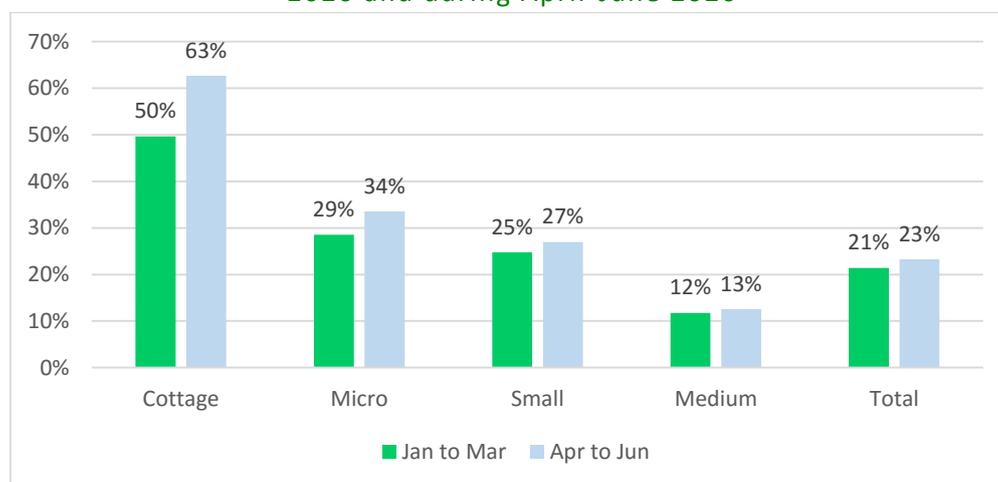
Eventually it became evident that banks and NBFIs will be preferring to provide credit to medium-sized entrepreneurs over smaller entrepreneurs. Taking this into account, Bangladesh Bank set up a special credit guarantee scheme solely for smaller entrepreneurs (cottage, micro and small entrepreneurs).

To monitor implementation of the CMSME stimulus package, Bangladesh Bank most recently has also directed the financiers to report their progress about providing credit to CMSMEs following a preset template. Through this initiative the central bank will be able to track progress utilizing disaggregated information (how much CMSME credit is disbursed in which areas and to what type of CMSMEs etc.).

Amid growing concerns about timely implementation of the CMSME stimulus package, Bangladesh has further eased certain requirements for Banks and NBFIs. For example, these financiers no longer need to disburse a mandatory share of the credit in rural areas. Requirements regarding following rigid ratios of manufacturing and service sector credits to total credit disbursed have also been revoked.

It is obviously too early to assess the positive effects of Bangladesh Bank's timely and flexible approach to safeguarding SME sector of the country. But still, it may be inferred that the financial sector regulator has chosen the most prudent approach given the current unprecedented situation. This indeed is a time for 'learning by doing'. However, recent data from Bangladesh Bank reveals a significant change in CMSME finance trends from pre-pandemic period to post-pandemic period. Apparently share of rural CMSME credit has increased since the introduction of the stimulus package.

Figure 12: Share (%) of rural CMSME loans in total CMSME loans during January-March 2020 and during April-June 2020



Source: Bangladesh Bank

Figure 12 shows that as a whole- credit to rural CMSMEs as share of total CMSME credit has increased from 21 percent to 23 percent from the first quarter of 2020 to the second quarter of 2020. There is similarly significant growth for all the sub-sectors (i.e. cottage, micro, small and medium enterprises).

While stakeholders in general are acknowledging the initiatives undertaken by GoB and Bangladesh Bank to safeguard SME sector during the pandemic, they are also concerned that the implementation of the stimulus package may prove to be more challenging than initially perceived (The Business Standard, 23 June 2020). It has been inferred by many stakeholders that despite significant easing of requirements, smaller entrepreneurs may still find it difficult to access much needed formal finance due to lack of cooperation from the Banks and NBFIs. More importantly, many feel that the government should provide further insight and guidance to the sector stakeholders to ensure better implementation of the stimulus package (ibid). In fact, many of the complex rules and regulations deserve to be simplified for the SMEs in particular to help them access the fund without much of a hassle. Indeed, the easing of the rules and regulations can itself be deemed as real stimulus by the SMEs. Latest data regarding disbursement of stimulus package credit to different sectors proves these fears to be true at least to a significant extent. For example, so far only 20 percent of the target regarding agriculture and SME credit disbursement has been achieved, whereas the ratio for larger industries has exceeded 70 percent.

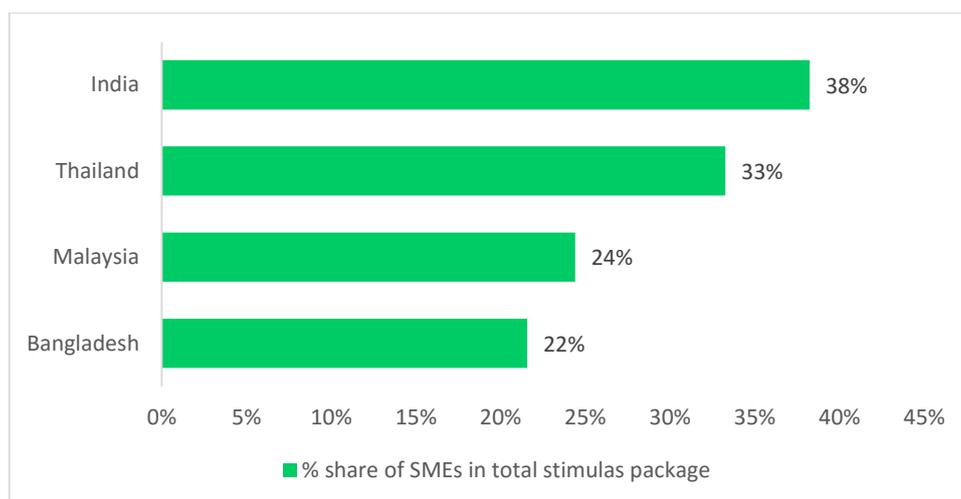
## 4. WAYS FORWARD

On the one hand, it is yet to be the time to predict an end to the ongoing global pandemic. And on the other hand, economies across the world need to reopen under the 'new normal' circumstances to safeguard macroeconomic achievements and to ensure resilience to further shocks. In this context, Bangladesh like every other country has started to gradually open up economic activities and has started implementing different policy interventions to protect different sectors and sub-sectors of the economy. While it is not the time yet to draw conclusions about the effects of CMSME stimulus package, the very nature of the current problem does not allow a 'wait and see' approach either. Along with 'learning by doing' on its own, Bangladesh also needs to review and analyze the SME policy responses of other countries.

### **SME POLICY RESPONSE: REVIEWING RECENT INTERNATIONAL TRENDS**

Due to obvious reasons, it is acceptable that size of stimulus package for Bangladesh SMEs be smaller compared to that of larger and/or more advanced economies such as Malaysia, Thailand, and neighboring India (size of Bangladesh SME stimulus package is USD 2.35 billion, and that of the said countries are USD 2.31 billion, USD 15.4 billion, and USD 13.0 billion respectively). However, the share of SME in total stimulus package (the ratio) should be more or less equal for all these countries (considering macroeconomic significance of SME sector for all of these comparable countries). This perhaps is where Bangladesh may be lagging.

**Figure 13: Share (%) of SME sector in total stimulus packages declared by Bangladesh and other comparable countries**



Source: LightCastle Partners, 2020

Figure 13 shows that Bangladesh intends to invest a meager 22 percent of the total stimulus package for its SME sector which is pretty close to Malaysia’s 24 percent. However, the country is significantly lagging compared to Thailand and India (33 percent and 38 percent respectively). This implies that most probably Bangladesh could have committed (financially) a bit more to safeguard its SME sector especially taking into account the contribution of the sector in employment generation and boosting domestic demand.

Like most other countries across the globe, Bangladesh has declared stimulus package for its SME sector to cope with the pandemic-induced economic slowdown and the package is comprised of flexible low-cost loans, refinancing schemes, and working capital finance. But the review by OECD of country responses to foster SME resilience has mapped a plethora of response measures that may be considered by Bangladesh policy makers and stakeholders in the coming days. Policy responses summarized by the said OECD report and having significant implications for Bangladesh SMEs safeguarding in the coming days are presented below:

**Table 2: Policy response in other countries to safeguard SME sector (OECD, 2020) and their implications for Bangladesh**

Policy response in other countries		Implications for Bangladesh
01)	Introduction of work time shortening, temporary lay-off, sick leave	Could be useful in case a second wave of COVID-19 attack takes place.
02)	Tax deferrals and public procurements	Could be especially useful in ensuring liquidity supply to smaller enterprises.
03)	Direct lending by public institutions and/or grants and subsidies	May be difficult given the resource constraints. But could be piloted for SMEs with comparatively constrained access to formal finance.
04)	Coming up with structural policies to help SMEs adopt new working methods	This is a must for safeguarding and promoting Bangladesh SMEs in the coming years (the ongoing

		digitization drive by GoB will ensure comparative advantage).
05)	Monitoring impacts and enhancing governance	Bangladesh lacks significantly in terms of maintaining SME database. This could be an opportunity to improve this, particularly when there is enough scope of using Artificial Intelligence for smart data management.

It should be adequately evident from Table 2 that Bangladesh has scope to go well beyond implementing stimulus packages to safeguard its SME sectors. Of course, impacts of these innovative policy measures are yet to be fully visible. But still Bangladesh may attempt to replicate few of these (upon contextualization) and the pilot them to see what works and what does not. A somewhat similar policy approach taken by Bangladesh Bank during the last global financial crisis ensured resilience and robust growth amid global economic slowdown.

### **POLICY RECOMMENDATIONS: LEARNING FROM OWN EXPERIENCE**

Along with learning from the international experiments, Bangladesh has a reach pull of experience of its own to learn from which could contribute towards better coping with the prevailing challenges. Some of those are discussed here:

#### SME POLICY 2019: STICKING TO THE PLAN

GoB's SME policy 2019 has rightly identified major challenges to SME sector growth in the country to be- 01) lack of access to finance, 02) Inadequate access to technology and innovations, 03) Absence of sufficient market linkage, 04) Insufficient human resource development, 05) low accessibility and low availability of business support services. The policy has clear directives and actionable programs to overcome these challenges. While these were relevant and timely before the pandemic, they have become even more so in the current situation. Hence, stakeholders should be most diligent in translating the commitments of this policy into viable actions with desirable outcomes.

#### INNOVATIVE COLLABORATION: UTILIZING THE BANK-MFI LINKAGE PROGRAM

Banks and larger NBFIs will remain to be less inclined to extend services to SMEs (especially to smaller ones located in hard to reach areas). MFIs on the other hand, have a proven track record of providing doorstep services to the hardworking and entrepreneurial marginal people across the country. They have also been successfully contributing to enhancing financial inclusion through working jointly with formal financial institutions. Policy makers could definitely opt for relying more on such bank-MFI linkage programs to extend finance and related supports to SMEs in the country.

#### ACCELERATING THE DIGITAL DRIVE: DFS AS THE NEW WAY

Growth of Digital Financial Service (DFS) especially in the form of Mobile Financial Service and Agent Banking has been exemplary in Bangladesh. As the central bank of the country embraced digital financial inclusion early on (over a decade ago), Bangladesh is already enjoying the fruits of digital finance. Reports from the grassroots suggest that people have been relying more on DFS during the pandemic-induced partial lockdown. Policy makers must opt to take this opportunity and further utilize digital finance to ensure adequate support the SMEs in the country.

#### TRACKING IMPLEMENTATION: IMPROVING GOVERNANCE

SME sector of the country has a complex composition and involves numerous stakeholder groups (from both public and private ends). While the central bank has already taken some initiative to monitor progress of implementation of the CMSME stimulus package, there is still much scope of improvement here. For example, a digital dashboard could be developed to ensure real time tracking of CMSME loan disbursement and recovery across the country. Top level policy makers could then easily monitor progress and revise/augment strategies as and when necessary. The central bank already has some experience regarding this and could build upon it.

#### ENHANCING EXPORT ORIENTATION: LOOKING FURTHER OUTWARD

While the SME sector of Bangladesh is already earning significant amount of foreign exchange through exports, there still remains a lot of scope to enhance exports. Of all the small enterprises 26 percent are engaged in export and the ratio for medium enterprises is 48 percent. In the post-pandemic many economies (advanced and developing alike) will be looking to new sources of import due changed geo-political realities. Bangladesh harness this opportunity and build capacity of its SME sector to boost export earnings. For that matter, there should be a more focused attention on better implementation of the stimulus for pre-shipment backward and forward linked SMEs involved in dyeing, washing, labeling, printing, packaging etc. In addition, the regulator should facilitate new kind of digital financing for the value chains in food processing including cold-chains and as well for all kinds of digital transformation by investing in people for e-learning, e-governance, e-health, e-commerce and out-sourcing etc. where smaller startups belonging to SMEs dominate.

#### **CONCLUDING REMARKS**

Bangladesh economy has done remarkably well especially over the last decade or so and a significant share of the credit for this may be attributed to this sector. However, the scope for further robust and sustainable growth of SMEs has already been identified as a pre-requisite to attaining the macroeconomic objectives. While the effect of the pandemic is yet to be as severe for Bangladesh economy as it has been for many other, the growth trajectory is facing a critical bump. And hence, accelerated and well-managed growth of SME sector has become even more critical for the country. Of course, the sector has started enjoying prudent policy attention most recently. Yet, stakeholders need to be as collaborative, coordinated and innovative as possible to translate these commitments into desired outcomes. Bangladesh is indeed a social laboratory for innovation, particularly in sustainable and inclusive financing. Let's hope it continues to remain so by riding on the success of SMEs which have huge potentials. Let these potentials be transformed into realities in the post-pandemic environment which may create new opportunities for small and medium entrepreneurs at large.

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